

Sales of services that are accompanied with the transfer of tangible personal property is subject to liability under the Service Occupation Tax Act. See 86 Ill. Adm. Code 140.101. (This is a GIL).

October 18, 2000

Dear Ms. Xxxxx:

This letter is in response to your letter dated July 5, 2000. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be accessed at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter, you have stated and made inquiry as follows:

BUSINESS has been authorized to represent a corporation (hereinafter the 'Company') in this Petition for Advisory Opinion regarding the services described below. Attached please find Illinois Form IL-2848, Power of Attorney, as duly executed by BUSINESS on behalf of the Company. We are requesting a determination on the following issues:

1. Whether the Company's planning services, which involve analyst consultation and research services, qualify as professional services not subject to Illinois sales and use tax; and
2. Whether the Company's reports, which are transferred as inconsequential elements of the service transaction, will subject any of the Company's charge for services rendered to the Illinois service occupation tax.

ACTIVITIES OF THE TAXPAYER

By way of background, the Company provides planning services and research information on communications and computing systems for various businesses based on each client's business needs. Through analyst-client interaction, the Company develops an understanding of each client's business and business needs in order to provide strategic planning assistance, technology forecasting, and cross-industry analysis. Typically, Company analysts provide 24 to 36 hours per year of interactive assistance by way of research and analysis to help with the development of a client's e-business ventures, enterprise networking, and Internet technology and electronic marketing initiatives.

The research information is provided to clients via an analyst-consultant, briefing sessions held at the clients' site, periodic research reports, weekly notes, conferences and audio conferences, and access to the Company's web site for electronic access to

research information. All the aforementioned components comprise the Company's subscription planning service and are sold for an annual subscription charge ranging from \$18,000--\$24,000. The following list details the components of its planning services.

- Analyst Interaction—24 to 36 hours per year (number of hours may change depending on the agreement). Clients can call and speak with a Company analyst regarding specific questions they may have. For example, a client may call with questions regarding new technology/software relevant to their business. An analyst will field the questions, perform research on the new technology/software, analyze the technology/software as it applies to the client's business, and provide answers and analysis to the client through phone discussions. Clients can also e-mail questions to the analysts and obtain verbal responses or by less preferred e-mail means.
- The Company Reports—Produced periodically (ranging from 18—24 reports throughout the year) by the Company. The reports generally encapsulate the advice given to clients. The reports are structured based upon questions posed by clients and the analysis performed by the Company's analysts to address these questions. The Company provides assessments of market structures, technologies, products and services, as well as practical assessments of developing industry trends and evaluations of emerging technologies. The finance department of the Company has determined that the per unit cost for a typical 20 page report is \$2.55.
- The Company Research Notes—A weekly e-mail publication. All subscribers get the same e-mail publication.
- Briefing Sessions--Company analysts meet with client at its offices or at client's location.
- Conferences—Free passes to 2 annual conferences sponsored by the Company.
- Audio Conferences—Clients can participate in quarterly conference calls conducted by company analysts. Slide presentations are available on the Company Web site and a RealAudio replay is posted after the event.
- Access IDs to the Company's Web site—Clients can download research reports and notes from the Company's web site.

The Company's planning and consulting services are much like that of tax, legal or other professional consulting services. Just as an accounting firm or a law firm is engaged by a client to perform research and analysis related to a question posed by the client, and provides oral advice or written documentation of the research and analysis conducted in the form of a memorandum or report, the Company is hired to provide a

multi-faceted service, which involves industry research and analysis as it relates to questions posed by its clients, strategic planning proposals, development and implementation of current technologies, and reports furnished in oral or written form.

All components are sold as a packaged subscription service and only analyst interaction time can be sold separately. The Company philosophy is for its sales force to sell analyst-consulting subscriptions. The value of the service provided lies with the consultation and analysis performed. When a customer signs up for the Company's service, the customer is purchasing the expertise and analytical skills of the Company's staff. However, on an isolated basis, the Company will provide research reports to non-subscribers only in instances in which it tries to entice a customer to subscribe to the planning or consulting services. In this regard, such reports are only provided on this limited promotional basis. It is never the Company's intention that it 'sells' such reports. Nor can a client merely subscribe to the Company for only receipt of such reports.

ISSUES

1. Whether the Company's planning services, that involve analyst consultation and research services, qualify as professional services not subject to Illinois sales or use tax?
2. Whether the Company's reports, which are transferred as inconsequential elements of the service transaction, will subject any of the Company's charge for services rendered to the Illinois service occupation tax?

SALES & USE TAX APPLICATION

1. Whether the Company's planning services, that involve analyst consultation and research services, qualify as professional services not subject to Illinois sales or use tax?

It is our interpretation that no sales or use tax is due on the services that the Company provides because services are generally not subject to sales or use tax in Illinois. The Company gathers its information by surveying, either via written questionnaires or telephone calls, its representatives in specific business industry sectors. This information is accumulated, analyzed, and discussed with industry representatives and clients to provide the basis for industry analysis, which is provided to the Company's clients.

Under a typical Company contract, the Company gathers and analyzes research based on the specifications of the Company's customer. Through analyst-client interaction, the Company develops an understanding of each client's business and business needs in order to provide strategic planning assistance, technology forecasting, and cross-industry analysis. Typically, Company analysts provide 24 to 36 hours per year of interactive assistance to a subscriber of its service, whereby the customer can telephone an analyst to address specific questions, or meet with analysts in person.

The analysts will gather information from the customer in order to perform a detailed analysis of the customer's specific business issue. The analysts will then present solutions specific to the customer's needs and requests, based upon the analysis performed.

The primary interest of the Company's clients is the consulting and planning services provided, in addition to the analysis performed on each client's business needs. In fact, the Company's planning services represent most of the Company's revenues, while the value of non-consulting services, such as periodic reports, represents an inconsequential amount of revenue for the Company. Accordingly, since the Company provides services and services are generally not subject to Illinois sales or use tax, the Company's services should not be subject to Illinois sales and use tax.

2. Whether the Company's reports, which are transferred as inconsequential elements of the service transaction, will subject any of the Company's charge for services rendered to the Illinois service occupation tax?

It is our interpretation that no sales or use tax is due on the services that the Company provides because services are generally not subject to Illinois sales or use tax. The Company's services also include the provision of periodic reports and electronic publications, which should not taint the tax treatment of the rendition of such services.

Generally, services are not subject to sales/use tax. However, a service occupation tax ('SOT') is imposed on tangible personal property transferred incidentally as part of a service transaction. The SOT applies to the selling price of the property transferred. 35 ILCS 115/3.

As stated, these reports and publications are inconsequential elements to the Company's primary focus, which is the provision of planning, consulting and research services. At times, it is the Company's intention that these reports serve as promotional material, which summarize the analysts' findings. Based on an analysis performed by the Company's finance department, the per unit cost for a typical 20 page report is \$2.55. Since the Company does not intend to separately 'sell' these reports, it does not have a standard selling price related to such reports.

Not unlike other professional consulting service firms, the Company typically does not separately state a charge for reports because its customers do not associate the cost of their subscription service to purchasing generalized industry reports. For example, an accounting or law firm may charge a client \$50,000 for consulting/compliance/legal services; however, these firms do not separately state a charge for a prepared tax return or client legal brief. Similarly, the Company provides a multi-faceted service, which involves industry research and analysis, strategic planning, and development and implementation of current technologies. As an added perk, the Company provides reports to its customers to keep them abreast of current trends. The reports are inconsequential to the actual services provided, which involves planning and consulting services by way of analyst interaction.

If the selling price of each item of tangible personal property transferred incident to a sale of service is not separately stated, the tax imposed will be based on 50% of the entire bill to the customer, but shall not be less than the cost price to the serviceman of the tangible personal property so transferred. *86 Ill. Adm. Code Sec. 140.101(e)*. If, however, the tangible personal property transferred incident to the sale of service is less than 35% of the total gross receipts from the transaction, the sale is not subject to the SOT. *86 Ill. Adm. Code Sec. 140.101(f)*.

Using the annual aggregate method for determining whether the tangible personal property transferred incident to the sale of service is less than 35% of the total gross receipts from the transaction, as proscribed by *86 Ill. Adm. Code Sec. 140.101(f)*, the company's services would not be subject to SOT. The total annual aggregate cost of parts transferred in the course of providing service, such as periodic reports and conference passes, is approximately 14% of the total annual aggregate receipts from the sales of service. As such, any tangible personal property transferred incident to the sale of service would not be subject to the Illinois SOT.

We hope that the above request will receive your full consideration. In this regard, please contact me at ##### if you have any questions or concerns. We look forward to working with the Department to resolve this matter expeditiously.

Thank you for your time and attention to this important matter.

The sale of planning or consulting services that is accompanied with the transfer of tangible personal property such as reports is subject to liability under the Service Occupation Tax Act. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred as an incident of their sales of service. Servicemen incur either Service Occupation Tax (SOT) liability or Use Tax liability in these transactions. The tax consequences depend upon the method used to calculate the liability. Servicemen may calculate their tax base in one of four ways: 1. separately stated selling price; 2. 50% of serviceman's entire bill; 3. SOT on his cost price if he is a registered de minimis serviceman; or, 4. Use Tax on his cost price if he is an unregistered de minimis serviceman. Please see the enclosed copy of *86 Ill. Adm. Code 140.101*, the Basis and Rate of the Service Occupation Tax.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale of service. The tax is then calculated on the separately stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may

qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred as an incident of the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations. Such servicemen collect a corresponding amount of Service Use Tax from their customers.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers.

You state that the cost of tangible personal property transferred in the course of your client's consulting services is approximately 14% of the company's total receipts from sales of service. So long as this is the case, the company would be de minimis and should employ either the third or final method explained above.

The provision of seminar materials such as non-customized materials or reports is generally subject to Retailers' Occupation Tax liability in Illinois. In your letter you say that the company may provide these gratis in order to entice new business. In these situations the company would incur a Use Tax liability. Please refer to 86 Ill. Adm. Code 150.305(c).

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Karl W. Betz
Associate Counsel

KWB:msk
Enc.